REPORT OF EXAMINATION
Western United Life Assurance Company
As of December 31, 1999

States Participating:
Washington
Oregon
Montana

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify based upon our examination, the Report of Examination shows the financial condition and business affairs of Western United Life Assurance Company of Washington, as of December 31, 1999.

Patrick McNaughton
Chief Examiner, Company Supervision

Date

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June 6, 2001
Olympia, Washington

The Honorable Kathleen Sebelius
Commissioner, Kansas Department of Insurance
NAIC Chair, Executive Committee
420 SW 9th Street
Topeka, KS 66612-1678

The Honorable Robert A. (Bob) Lohr
NAIC Secretary, Western Zone
Commissioner, State of Alaska
Department of Community & Economic
Division of Insurance
PO Box 110805
Juneau, AK 99811-0805

The Honorable Mike Kreidler
Insurance Commissioner
State of Washington
Insurance Building
PO Box 40255
Olympia, WA 98504

Dear Commissioners:

In accordance with your instructions and in compliance with the statutory requirements, an association examination has been made of the corporate affairs and financial records of

Western United Life Assurance Company
of
Spokane, Washington

hereinafter referred to as the "Company" or "Western" at its home office located at 916 West First Avenue, Spokane, Washington 99201. This report of examination is respectfully submitted showing the financial condition of the Company as of December 31, 1999.

SCOPE OF EXAMINATION

Our examination was conducted on a full scope basis and included all the business affairs and financial condition of the Company for the six year period ending December 31, 1999. The examination was performed in accordance with procedures promulgated by the National Association of Insurance Commissioners (NAIC) and in compliance with the provisions of Washington state insurance laws and regulations. The Company was last examined as of December 31, 1993 by examiners from the states of Washington and Idaho. Any comments or findings noted during the examination are summarized in the "Instructions" and/or "Comments and Recommendation" sections of this report.

INSTRUCTIONS

1. Form D filings -Prior Approval

The Company had numerous intercompany transactions with Metropolitan Mortgage & Securities Company, Incorporated (Metropolitan) and other affiliates that required prior approval under RCW 48.31B.030(1)(b). These transactions consisted of sales and purchases of securities, mortgages, affiliate loans and other invested assets some of which exceeded three percent of prior year's admitted assets or $26.57 million.

The Company is instructed to comply with the statutory provisions in the Insurer Holding Company Act, specifically RCW 48.31B.030, which requires prior approval of transactions consisting of sales and purchases of securities, mortgages, affiliate loans and other invested assets which exceeded three percent of prior year's admitted assets.

2. Form B filings - Notification

Interrogatory 12 discloses $20.9 million in loans to stockholders. The loans were made to the parent, Metropolitan for mortgage loan purchases. These mortgages are used as collateral for the loans. Western lists the collateralized mortgages as assets on schedule B to offset the loan to Metropolitan.

RCW 48.31B.025(c) requires the Company to report the loans on an amended Form B when the .5% threshold is met to keep current the information disclosed in its registration statement by reporting all ***material changes*** or additions within fifteen days after the end of the month in which it learns of each change or addition. RCW 48.31B.025(4) defines ***Material*** as any amount greater than ½ of one percent of prior years admitted assets. The material changes are reported as an amendment to Form B per WAC 284-18-410. ½ of one percent of Western's prior year's admitted asset equaled $4.428 million.

In addition, Western had numerous other transactions with affiliates in 1999 which exceeded the ½ of one percent threshold or were specifically required for prior notification under RCW 48.31B.025, and were not properly amended and filed on Form B. These are as follows:

- i.) The Company sold annuitized receivables to Metropolitan, $4,629,141.
- ii.) The Company purchased securities from Old Standard Life, $6,030,000.
- iii.) The Company sold securities to Metropolitan, $9,705,696.
- iv.) The Company made collateralized loans to Metropolitan, $7,000,000.
- v.) The Company received payments on collateralized loans to Metropolitan, $14,000,000.
- vi.) The Company purchased mortgage loans from Old Standard Life, $15,056,084.
- vii.) The Company purchased mortgage loans from Old West Annuity and Life, $11,581,177.
- viii.) The Company made a commercial mortgage loan to Metropolitan, $12,000,000.
- ix.) The Company paid Metropolitan $622,708 in dividends on preferred stock under solicitation permit #301 which were not submitted for prior notification pursuant to RCW 48.31B.025(5).

The Company is instructed to comply with the statutory provisions of the Insurer Holding Company Act, specifically RCW 48.31B.025, which requires filing an amended Form B per WAC 284-18-410 for all transactions between Western and affiliates which exceed individually ½ of one percent, or at such point like transactions total ½ of one percent in annual cumulative total.

3. Unrecorded Liabilities

Except for taxes, licenses and fees, the Company has treated unpaid expenses on a cash basis. No accruals were made for general operating expenses, accrued vacation benefits and other expenses incurred but still outstanding as of December 31, 1999. The NAIC Annual Statement Instructions, Exhibit 5, and RCW 48.12.030(5) require accrual of all taxes, expenses, and other obligations at the date of the statement.

Our review judgmentally selected all administrative and investment related expenses, excluding investment sales and purchases, that were greater than or equal to five thousand dollars through the first three months of year 2000. Items related to recurring payments to vendors and affiliates were tested only in January 2000. Our sample disclosed Western had material expenses that were not accounted for in a year end accrual. These areas included vacation time, professional services and miscellaneous general expenses.

The Company is instructed pursuant to RCW 48.12.030(5), to report unpaid general expenses using the accrual method on Exhibit 5. In addition, an adjustment for the unpaid general expenses is required to accurately reflect expenses in the year of occurrence under the accrual method. The following adjustment is required to accurately reflect general expenses due and accrued in our examination report:

	Dr	Cr
General Insurance Expenses	**$281,829**	
General Expenses Due or Accrued		**$281,829**

4. Federal Income Tax Recoverable

Our examination reviewed the Company's federal income tax and corresponding federal income tax recoverable for the period ended December 31, 1999. Our review indicated the Company under accrued federal income tax recoverable by $629,797. This was mainly due to structured lottery settlements bought from states which withheld federal income taxes from proceeds during the year. These prepayments of federal income taxes were under estimated when the recoverable was posted by the Company. Our testing tracked the subsequent refund and deposit of the proceeds in the Company's bank account.

The Company is instructed to properly identify, estimate and report federal income tax recoverable. This will ensure full and adequate accounts and records of its assets, obligations, transactions, and affairs in compliance with RCW 48.05.280 and enhance the credibility and accuracy of future statutory and other filings. In order to properly reflect the federal income tax recoverable in our examination report, the following adjustment was required:

	Dr	Cr
Federal Income Tax Recoverable	**$629,797**	
Federal Income Taxes Incurred		**$629,797**

5. Annual Shareholders Meeting

Review of the annual shareholders minutes for the period under examination disclosed the Company was not in compliance with RCW 48.07.040 which requires an annual shareholders meeting within the first four months of the year. It was noted in our review that in several years under examination the annual shareholder meetings were held after the first four months of the year.

Pursuant to RCW 48.07.040, the Company is instructed to hold annual shareholders meetings within the first four months of every year.

6. Mortgage Loan Guarantee

Metropolitan using its market contacts, expertise and personnel locate investment grade receivables for the benefit of Western. These receivables consist of structured settlements, lotteries and mortgage loans which meet statutory guidelines. All investment grade receivables purchased between September 1993 through March 1998 are guaranteed by Metropolitan as to performance and yield. Metropolitan provides a yield guarantee that approximates a net yield equivalent to the risk free rate at the time of acquisition. Western pays Metropolitan an acquisition services fee for this guarantee which is calculated using a mutually agreed upon expected life.

In order to assure faithful performance of this guarantee, the agreement specifies Western to hold back a reserve from the acquisition services fee based on the present value of the expected losses over the expected life of the receivable(s). The loss reserve is carried as a liability by Western and is debited when losses are realized on guaranteed receivables that have defaulted. Interest due on receivables in default, but not yet disposed, is also required to be paid by Metropolitan. In 1999, Metropolitan paid $1,076,771 in interest to Western on receivables in default.

The Company had approximately $261,493,157 in outstanding receivables subject to the guarantee as of 12-31-99, consisting of $93,299,301 and $168,193,856 of mortgages and structured settlements, respectively. The Company recorded an obligation of $2,358,000 and $8,519,000 associated with the loss reserve at December 31, 1999 and 1998, respectively. The reserve is only an estimate and Metropolitan is required to compensate Western for any amounts exceeding the loss reserve. Losses exceeded the reserves in 1999 by $1,752,043. Metropolitan did not settle the difference nor was it recorded as an intercompany receivable. Two instructions are required to bring the Company into compliance:

a. Intercompany Receivable

In 1999, the loss reserve was deficient by $1,752,043. This deficiency was not recorded as a receivable by Western or as a payable by Metropolitan nor was the reserve increased. The intercompany receivable to Western should have been increased by $1,752,043. Consequently, Metropolitan should have recorded an intercompany payable of $1,752,043. These amounts should be settled on a quarterly basis or other reasonable basis as stated in the intercompany agreement.

Pursuant with RCW 48.05.250 and WAC 284-07-050(2), which states,

> "To effectuate RCW 48.05.250,…and to enhance consistency in the accounting treatment accorded various kinds of insurance transactions, the valuation of assets, and related matters, insurers shall adhere to the appropriate Annual Statement Instructions and the Accounting Practices and Procedures Manuals promulgated by the NAIC."

The NAIC Accounting Practices and Procedures Manual for Life, Accident and Health Insurance Companies states,

> "To the extent that the affiliate has liquid assets with which to repay the balance, and to otherwise maintain its account on a current basis, the amount may be admitted."

Pursuant to RCW 48.05.250, the Company is instructed to book and collect all amounts due on the assets covered under the guarantee when realized on a quarterly or other reasonable basis as stated in the intercompany Management, Acquisition and Servicing Agreement. The required examination adjustment is as follows:

	Dr	Cr
Receivable from Parent, Subsidiaries and Affiliates	**$1,752,043**	
Unassigned Funds		**$1,752,043**

b. Holdback Reserve

Western is instructed pursuant to RCW 48.31B.030(1)(a)(iii) to seek specific performance under the agreed upon terms of the intercompany agreement. Under performance of the contract, Metropolitan and Western need to estimate and establish a loss reserve which would be required to cover the present value of expected losses over the remaining expected life of those remaining receivables under the agreement. See instruction 18 Accounts, Records and Internal Controls for additional instruction.

7. Home Office Capitalized Non-Admitted Assets

The Company is not in compliance with RCW 48.12.020 ("Nonallowable assets"). This requirement states that the following expressly shall not be allowed as assets in any determination of the financial condition of an insurer: furniture, furnishing, fixtures, safes, equipment, vehicles, library, stationery, literature, and supplies. PriceWaterhouseCoopers (PWC) did some testing of the additions to the property and vouched them to their respective invoice and check copy. The invoices indicated items such as carpet, chairs and file drawers, which under statutory accounting are non-admitted assets. The examiners retested and relied on PWC's work.

Based on RCW 48.12.020, the Company is instructed to non-admit furniture, furnishing, fixtures, safes, equipment, vehicles, library, stationery, literature, and supplies. The following adjustment is required to exclude these assets from Home-office Real Estate account for statutory purposes:

	Dr	Cr
Change in Non-Admitted Assets	**$100,759**	
Properties Occupied by the Company		**$100,759**

8. Investment Real Estate

Our review of Investment Real Estate disclosed several areas of non-compliance with Washington statutes and the NAIC Annual Statement Instructions. The Company is instructed to correct the deficiencies noted and institute adequate controls to insure compliance in the future. The exceptions noted and instructional remedies are as follows:

a. Capitalized expenses

Review of the 1999 capitalized development expenditures noted that many of the items that were being capitalized, and therefore added to the properties value, should have been expensed. These included such items as advertising, landscape maintenance, commissions paid to agents for leasing the properties to various tenants, and legal fees related to leasing the properties. Our examination identified $515,402 of capitalized expenditures which should have been expensed in order to eliminate the capitalization of lease fees and in-house commissions.

RCW 48.12.190 (Valuation of Property) states:

> "real property acquired pursuant to a mortgage loan or a contract for a deed, in the absence of a recent appraisal deemed by the commissioner to be reliable, shall not be valued at an amount greater than the unpaid principal of the defaulted loan or contract at the date of such acquisition, together with any taxes and expenses paid or incurred in connection with such acquisition, and the cost of improvements thereafter made by the insurer…"

Furthermore, the NAIC Accounting Practices and procedures manual states:

"Repairs and maintenance expenditures may be classified as ordinary or extraordinary. As a general rule, expenditures for ordinary repairs that are necessary to put assets back into good operating condition, and for maintenance to keep them that way are expensed as they are incurred. Extraordinary expenditures which add to or prolong the life of the property should be capitalized."

The Company is instructed to review capitalized costs to properly classify these as items to be expensed or capitalized in a manner prescribed by the NAIC Accounting Practices and Procedures Manual pursuant to RCW 48.05.250 and WAC 284-07-050(2). The following adjustment is required to reduce investment real estate and expense costs that should not have been capitalized:

	Dr.	Cr
General Insurance Expenses	**$515,402**	
Investment Real Estate		**$515,402**

b. Title insurance

Our examination of real estate purchased by the Company from Metropolitan for future development revealed that evidence of title insurance could not be verified on several of those properties. Metropolitan could not produce any evidence of title insurance, only title insurance commitments were available for review. No evidence was available to substantiate that title commitments were used to issue title insurance.

Pursuant to RCW 48.05.280, the Company is instructed to enhance its controls and oversight on investment real estate in order to properly obtain title insurance and identify encumbrances that would diminish the value and ownership of assets pursuant to RCW 48.13.130 which defines an encumburance.

c. Annual Statement Schedule A

The NAIC Annual Statement Instructions describe how to correctly report real estate on Schedule A - Part 1. The Company did not comply with the instructions in several areas as follows:

Column 4 – The Company incorrectly reported the year of last appraisal for all the properties. Furthermore, it reported properties with appraisals in which no evidence of appraisal could be verified.
Column 9 – The Company failed to report increases by adjustment in book value during the year. It should have reported the 1999 capitalized development expenditures.
Column 11 – The Company failed to report amounts received from real estate sales during the year. Our review indicated that two investment properties, Airway Business Center and Liberty Lake Center, had partial sales during 1999 that should have been reported in column 11.
Column 13 – The Company understated 1999 gross income earned by $103,022. The reported amount on Schedule A – Part 1 was $258,501. However, supporting detail indicated total 1999 rents due of $361,523. Furthermore, it failed to correctly apportion the amounts to the various properties.

The Company is instructed to correct all deficiencies noted above and institute written guidelines that are periodically reviewed for adherence. This will ensure full and adequate accounts and records of its assets, obligations, transactions, and affairs in compliance with RCW 48.05.280 and WAC 284-07-050(2) to enhance the credibility and accuracy of future statutory and other filings and comply with NAIC Annual Statement Instructions. The above deficiencies were not all inclusive, but were deemed significant enough for separate mention.

d. Appraisals

The Broadmoor and Spokane Valley properties were not appraised when purchased by the Company. The December 31, 1999 book value for these properties totaled $6,526,725 or approximately 31% of the book value of investment real estate. RCW 48.13.140(1) states, "The fair value of property shall be determined by appraisal by a competent appraiser at the time of the acquisition of real property..." When the properties were transferred from Metropolitan to Western United, an appraisal was not performed. Several of the properties have never had an appraisal, which made it more difficult to verify their value (and original cost) at the time of transfer.

The Company is instructed to obtain appraisals on these properties in order to more accurately determine their value pursuant to RCW 48.13.140.

9. Mortgage Loans

An extensive review of the Company's mortgage loan portfolio for the year end December 31, 1999 was performed in the course of our audit. During our initial testing of the mortgage loan portfolio, a modified probability proportion to size (PPS) methodology was used to sample the portfolio (suspense pools eliminated). This sample indicated material compliance issues regarding lack of assignments (ownership) and minor incidences of title insurance and loan to value exceptions. The lack of assignments noted in the exceptions were mainly due to the high annual turnover rate within the mortgage loan portfolio (145%) and intercompany pooling to effectuate secruitization activity.

Because of the material exception rates on lack of assignments obtained in the modified PPS sample it was determined that Control Reliance would have to be lowered to medium from high and a new PPS (not modified) sample including suspense pools would be conducted targeting assignment compliance to generate an extrapolated examination adjustment. Our reliability factor doubled which decreased the selection interval by half or $2.5 million to $1.25 million. This increased our sample size from one hundred and forty loans to two hundred and eighty-four loans, and according to PPS sampling techniques, gave us a ninety-five percent overall examination assurance of representing the population as a whole. The two hundred and eighty-four loans had a statement value of approximately $68.5 million or 17.4% of the total population of $392,897,608.

The results of the second PPS sample indicated the Company had material control deficiencies in its ability to track and monitor assignment activity in order to perfect clear title to its purchased mortgage loans. From the two hundred and eighty four mortgage loan files tested, ninety-three or approximately $16.1 million in statement value were missing the required assignments to Western. This equates to an exception rate of approximately 23.5%, which when projected on the entire population would require an adjustment to statement value of approximately $92.5 million.

When these findings were disclosed to the Company, it immediately devoted considerable time and resources to set up a task force to manually review all of the approximately $380 million in outstanding mortgage loans as of December 31, 2000. Additionally, a meeting with Metropolitan's and Western's officers and directors was held in Spokane to assure the Commissioner's Office that all assignments on the Company's mortgage loans would be perfected before the end of the field work. The Company Officials also guaranteed that proper controls consisting of written guidelines, enhancements to tracking and monitoring systems, ongoing training programs, accountability, real time status and reporting, periodic internal audits and ongoing review to improve on the processes would be instituted.

The Insurance Commissioner's Office agreed to conduct a third and final sample on the December 31, 2000 mortgage loan population using the same criteria as in sample two with the understanding that if the Company could adequately demonstrate all assignment exceptions were corrected and the new and enhanced controls were documented and functioning as designed, no adjustments would be made in the 1999 examination report.

Using the same PPS criteria in sample three as in sample two, we tested approximately 25.4% or $96.4 million of the December 31, 2000 outstanding mortgage loan balance. No exceptions were noted in our review. All files sampled were adequately documented with a recorded perfected assignment, or independent proof was obtained that they were in the process of recordation with the appropriate county recording agencies. Additionally, the control enhancements were reviewed for adequacy, and certain selected controls were reviewed and verified as to implementation and reporting ability. No problems were noted and the control improvements appear to adequately meet our audit objectives and the Company's stated operational objectives above. Based on our review of mortgage loans the Company is instructed to comply with the following:

a. Assignments and title insurance

No audit adjustment is recommended for our examination report. The Company is, however, instructed to continually monitor controls and processes and to perform internal audits on mortgage loans and other real estate investments to ensure title insurance is obtained and assignments are recorded in a timely manner, perfecting legal title, and complying with RCW 48.12.010 which states:

> **"In any determination of the financial condition of any insurer there shall be allowed as assets only such assets as belong wholly and exclusively to the insurer, which are registered, recorded, or held under the insurers name.."**

b. Loan to value ratios

RCW 48.13.120, requires certain guidelines that limit investments in property to seventy-five percent of fair value, eighty percent of single family residential market value, or ninety percent of the fair value of purchase money mortgages. In our initial sample of mortgage loans, exceptions were noted in loan to value ratios that exceeded the required maximum allowable. The Company defended these exceptions as compliant either by reason of the SMMEA exemption or a "Participation Agreement" with Metropolitan.

The Company does not have a formal Insurance Commissioner's Office (ICO) approved intercompany Participation Agreement nor was any internal agreement available for review. Our analysis and review did not recognize either as defensible due to the SMMEA analysis conducted under instruction ten below, and the inability of the Company to produce a valid ICO approved intercompany Participation Agreement. No examination adjustment was deemed necessary but the Company is instructed to comply with the following:

Pursuant to RCW 48.13.120, the Company is instructed to enhance controls to ensure compliance with, **and to non-admit all balances that exceed the loan to value requirements. The Company is instructed to review all existing files to identify and non-admit all non-conforming loan to value balances and refrain from purchasing any loans that do not meet the statutory guidelines.**

Pursuant to RCW 48.31B.030(1)(b)(iv), the Company is instructed to formalize and submit for approval to the Insurance Commissioner's Office any participation agreement the Company chooses to utilize in order to reserve for or mitigate against non-compliant loan to value mortgage loans. Until such time of approval, no credit will be given for any participation or reserved funds which are not specifically segregated and earmarked for this specific purpose.

10. Secondary Mortgage Market Enhancement Act of 1984 (SMMEA) Exemption

The Company had approximately $60 million in mortgage loans as of December 31, 1999 for which it claimed an exemption to RCW 48.13.265 under the Secondary Mortgage Market Enhancement Act of 1984. RCW 48.13.265 limits domestic insurers investments in real estate, real estate contracts, and notes, bonds and other evidences of debt secured by mortgages on real estate to sixty-five percent or less of the insurer's assets. This statute was designed to limit an insurer's overall asset risk in real estate backed investments and ensure a balanced risk profile in order to safeguard company assets backing policyholder policy commitments. Without the SMMEA exemption, the Company is over the 65% limitation.

The department recognizes the validity of the SMMEA Exemption contained in 15 USC. However, our review indicated the Company uses very basic procedures within its mortgage loan system to identify exempted mortgage loans under SMMEA. The Company could not supply adequate documentation to support all SMMEA provisions to allow for the exemption from Washington State law for these assets. For example, support was not always available to demonstrate that the securities were rated in one of the two highest rating categories by at least one nationally recognized statistical rating organization. Or, evidence that the notes were originated by a savings and loan association or bank supervised by a state of federal agency. Nor, did the Company supply evidence of aggregate purchase prices of more than $250,000 for each block.

The Company has obtained an opinion from outside counsel regarding legal compliance with the SMMEA code. Counsel indicates that in order for the Company to claim SMMEA exemptions for assets (1) the note or notes must be secured by a first lien on residential or commercial real property, (2) the note or notes must have been originated by a savings and loan association or bank supervised by a State or Federal agency, (3) the sales price of the note or notes must have been for your own account. In the examiners' opinion, the Company has not performed enough due diligence to ensure that all of these tests have been met.

Subsequent to the examination date and during the period of our examination work when this issue was under review, the Company voluntarily reduced assets backed by real estate in an effort to come into compliance in the eventuality of an unfavorable disposition on the application of the SMMEA preemption of state law. Western is in compliance with RCW 48.13.265 without the SMMEA exemption as of December 31, 2000. The Company has acted in good faith during the course of the Insurance Commissioner's Office review, interpretation and final disposition of the issue. Due to this, no adjustment is recommended to non-admit the portion that exceeds the sixty-five percent limitation as of December 31, 1999.

Western is instructed to maintain sixty-five percent or less of its assets in real estate, real estate contracts, and notes, bonds and other evidences of debt secured by mortgage on real estate in compliance with RCW 48.13.265. The SMMEA preemption of state law should only be applied to mortgage backed securities that meet the Title 15 USC requirements. The Company is further instructed to comply with RCW 48.05.250 to ensure adequate accounts and records are maintained to demonstrate compliance with all provisions of this Code.

11. Guarantee Fund Assessments

The Company has reasonably assessed the amount of guarantee funds required to fund insurance company failures in the various states it conducts business. Because this assessment is probable and estimable it should have been accrued. It failed to post an accrual for this expense and an adjustment is required to properly reflect the liability in its financial statements. The NAIC Annual Statement Instructions require guarantee fund assessments to be accrued as a liability on Line 14, taxes, licenses and fees due or accrued.

Pursuant to RCW 48.12.030(6) and the guidelines set forth in the NAIC Annual Statement Instructions, the Company is instructed to accrue all guarantee fund assessments that are probable and estimable. The following adjustment has been made for the examination financial statements:

	Dr.	Cr.
Insurance Taxes, Licenses and Fees	**$1,832,639**	
Taxes, Licenses and Fees due or Accrued		**$1,832,639**

12. Commissions to Officers and Directors

The Company paid commissions to three officers of the Company. The commissions are immaterial but the Company is instructed to cease this practice due to the appearance of conflict of interest. This was also noted in the previous examination, but the Company failed to correct the problem by using other means of remuneration which are not based on commission scales due to the sale of insurance. The following is a list of commissions paid in1999:

John Van Engelen	President	185
Dale Whitney	VP	144
Scott Cordell	VP	3,428

Pursuant to RCW 48.07.130, "...no officer or director of an insurer shall accept, except for the insurer, or be the beneficiary of any fee, brokerage, gift, commission, or other emolument because of any sale of insurance...". The Company is instructed to cease all commissions to officers of the Company per RCW 48.07.130.

13. Intercompany Payable

It was noted in our review that general ledger account #19366, Metropolitan/Western contract purchases, is used almost exclusively for advances of cash to Metropolitan for the purchase of mortgage or contract receivables. The activity in this account has increased dramatically since the Company has participated in the securitizations over the past several years. Theoretically the advances should be for mortgage loans that are subject to purchase currently by Western. Our review indicates the advances are used more as a short term borrowing tool or line of credit by Metropolitan for all of its mortgage acquisitions. Those loans meeting the statutory guidelines are transferred to Western and are used to pay down the line of credit.

This particular arrangement allows Metropolitan to borrow money from Western on a short term basis and does not provide for interest on loaned funds. During 1999, Western transferred money almost on a daily basis while Metropolitan generally reimbursed once or twice a month. This allowed Metropolitan to effectively have an unsecured interest free line of credit. These transactions would not be fair and reasonable outside of the holding company arrangement.

Pursuant to RCW 48.31B.030(1)(a), "Transactions within a holding company system to which an insurer subject to registration is a party are subject to the following standards:

(i) The terms must be fair and reasonable;
(ii) Charges or fees for services performed must be fair and reasonable;…"

The Company is instructed to formalize an agreement for this intercompany borrowing arrangement which includes a provision to assess Metropolitan a fair and reasonable market rate of interest and to have it approved by the Office of the Insurance Commissioner pursuant to RCW 48.31B.030. The Agreement must be fair and reasonable as required by RCW 48.31B.030, and if the annual cumulative total of the loans to Metropolitan exceed the three percent of prior year's admitted assets it must be approved pursuant to RCW 48.31B.030(1)(b). See Instruction 18 Accounts, Records and Internal Controls.

14. Life Insurance Premiums and Annuity Considerations Deferred and Uncollected

In determining this asset, the Company failed to subtract the due and unpaid premiums on its life reinsurance. The net effect of recognizing these premiums is a $36,032 decrease to Life Insurance Premiums and Annuity Considerations Deferred and Uncollected.

To ensure full and adequate accounts and records of its assets, obligations, transactions, and affairs in compliance with RCW 48.05.280 and WAC 284-07-050(2), the Company is instructed to include premiums payable on reinsurance ceded when determining due and deferred premiums on its life insurance policies. The following adjustment is required to properly reflect the true balance of Life Insurance Premiums and Annuity Considerations Deferred and Uncollected:

	Dr.	Cr
Unassigned Funds (Surplus)	**$36,032**	
Life Insurance Premiums and Annuity Considerations Deferred and Uncollected		**$36,032**

15. Aggregate Reserve for Life Policies and Contracts

Our review of Aggregate Reserve for Life Policies and Contracts indicated several areas requiring adjustments as described below. The following computational adjustments were made to Aggregate Reserve for Life Policies and Contracts to reflect our findings in the actuarial review:

a. Level-Term Reserve

We estimated revised reserve factors for level-term policies that reflect the dynamic valuation interest rates found in the Standard Valuation Law. **Our revisions result in a $349 increase to aggregate life insurance reserves.**

b. ART Reinsurance Ceded Reserve

We estimated appropriate reinsurance ceded reserve credits for basic, sub-standard, and deficiency reserves for the Company's coinsured annual renewable term policies. **Our changes result in a $95,039 decrease to aggregate life insurance reserves.**

c. Non-Deduction Reserve

We recalculated the reserve for the non-deduction of deferred fractional premiums to reflect all deferred premiums for individual policies. **Our changes result in a $920 increase to aggregate life insurance reserves.**

d. Immediate Payment of Claims Reserve

Actuarial Guideline XXXII calls for the Immediate Payment of Claims Reserve to be calculated using one-third of one year's valuation interest rate when a Company's policy forms provide for the immediate payment of death proceeds without an interest adjustment. We recalculated the Immediate Payment of Claims Reserve on individual policies. **Our recalculation results in a $200,066 decrease to aggregate life insurance reserves.**

e. "Change in Funds" Recalculation

We recalculated the reserve for deferred annuity plans valued using the "Change in Funds" reserving methodology**. Our recalculation results in a $165,706 increase to aggregate life insurance reserves.**

f. Reserves Released on Annuity IBNR Claims

We used the Company's paid claims experience through June 30, 2000, together with an estimate of remaining payments on claims incurred prior to December 31, 1999, to recalculate the reserves released on claims incurred but not reported (IBNR) to the Company for individual deferred annuities, net of reinsurance ceded. **Our recalculation results in a $1,789,789 decrease to aggregate life insurance reserves.**

g. Recalculation of Deferred Annuity Reserves

The Standard Valuation Law (SVL) defines the methods and assumptions that are to be used for determining minimum statutory formula reserves for deferred annuity contracts. The SVL-defined methodology for annuity contracts -- the Commissioners Annuity Reserve Valuation Method (CARVM) -- requires that "reserves be the greatest of the respective excesses of the present values, at the date of valuation, of the future guaranteed benefits, including guaranteed non-forfeiture benefits, provided for by such contracts at the end of each respective contract year, over the present value, at the date of valuation, of any future valuation considerations … that become payable prior to the end of such respective contract year."

Actuarial Guideline 33, initially effective on December 31, 1995, provides an interpretation of CARVM, and a suggested methodology for calculating the minimum statutory formula reserves. Actuarial Guideline 33 was revised effective December 31, 1998. The revised guideline provides a more explicit interpretation of the CARVM reserves, including the concept of determining the reserves using an Integrated Benefit Stream Approach.

Prior to December 31, 1998 the Company calculated the formula reserves for its deferred annuity contracts using a conservative interpretation of CARVM consistent with existing industry practices and methods. The Company continued to use this methodology to calculate the reserves reported in both the 1998 and 1999 Annual Statements. Recently, the Company implemented a reserving methodology consistent with the requirements of the revised Actuarial Guideline 33. We reviewed the Company's re-calculation of the December 31, 1999 reserves for its deferred annuity contracts using the revised methodology. Based on the recalculation, the reported deferred annuity reserves should be reduced by $4,681,998.

The net effect of these adjustments is a $6,599,917 decrease to the Aggregate Reserve for Life Policies and Contracts which is reflected in the following adjustment:

	Dr.	Cr.
Aggregate Reserve for Life Policies and Contracts	**$6,599,917**	
Unassigned Funds (Surplus)		**$6,599,917**

16 Life Policy and Contract Claims

The reported Life Policy and Contract Claims liability is comprised of due and unpaid pending claims, and an estimate of IBNR claims as of December 31, 1999. The Company's paid claims experience through June 30, 2000, together with an estimate of remaining payments on claims incurred prior to December 31, 1999, indicates that the reported liability for IBNR claims for individual deferred annuities, net of reinsurance ceded, is understated by $1,802,682. The following adjustment is required to accurately reflect the Life Policy and Contract Claims liability as of December 31, 1999:

	Dr.	Cr
Unassigned Funds (Surplus)	**$1,802,682**	
Life Policy and Contract Claims		**$1,802,682**

17. Exhibit 8 – Reporting Deficiencies

The Annual Statement Instructions call for deferred annuity contract reserves to be categorized by year of issue, valuation mortality table, and valuation interest rate in Exhibit 8, Part B. The Company's presentation in the 1999 Annual Statement categorizes all pre-1998 issues under the 1971 IAM mortality table. Since the 1983(a) mortality table is the required valuation mortality table for much of this period, the presentation suggests that the Company incorrectly calculated the reserves on its deferred annuity contracts.

However, our review found that the Company did not use an incorrect mortality table in calculating the formula reserves for its deferred annuity contracts. The presentation in Exhibit 8, Part B is not a true representation of the Company's reserve calculation. The referenced 1971 IAM mortality table is the mortality basis for the guaranteed annuitization rates found in the Company's deferred annuity contracts that were issued during the 1970's and early 1980's. In the 1980's, the Company changed the mortality basis of the guaranteed annuitization rates to the 1983(a) mortality table. The Company failed to update the presentation of reserves in Exhibit 8, Part B to reflect this change. The mortality table that was used to determine the guaranteed annuitization rates does not directly enter into the Company's calculation of the formula reserves. The reported reserves were calculated as the greatest present value of guaranteed nonforfeiture benefits. This calculation does not involve the use of a mortality rate assumption. In all cases, the Company found that this reserve exceeded the present value of the annuitization benefits.

The Company is instructed to correct the reporting deficiency noted above. This will ensure full and adequate accounts and records of its assets, obligations, transactions, and affairs in compliance with RCW 48.05.280 and WAC 284-07-050(2) to enhance the credibility and accuracy of future statutory and other filings and comply with NAIC Annual Statement Instructions.

18. Accounts, Records and Internal Controls

Accounts, records and internal controls were found to be adequate in all areas except intercompany activity. Our examination of intercompany accounts and records disclosed weakness in several areas of the Company's intercompany transactions and operations as well as inadequate documentation of intercompany transactions as support for financial records. Testing and sampling techniques performed during our fieldwork were adjusted to compensate where feasible for the weaknesses detected. In some instances, the balances could not be substantiated by our audit or by the Company. It was determined that the weaknesses did not appear to materially effect the Company's financial statements, but this could not be reasonably verified. The problems disclosed during our audit were related to inadequate written documentation on procedures and guidelines, and turnover of key personnel.

The Company is instructed to correct all deficiencies noted below and institute written guidelines that are periodically reviewed for adherence. This will ensure full and adequate accounts and records of its assets, obligations, transactions, and affairs in compliance with RCW 48.05.280 and enhance the credibility and accuracy of future statutory and other filings. The following deficiencies are not all inclusive, but are deemed significant enough for separate mention:

a. Intercompany transactions and agreements

The Company has numerous material intercompany financial relationships and transactions in its normal course of business. Existing intercompany agreements do not adequately cover the fiduciary and other responsibilities under the various intercompany relationships. Our examination noted several accounts and transactions which could not be verified as consistent, fair and reasonable pursuant to RCW 48.31B.030(1)(a). The following areas were identified in the course of our examination and require amendments to the formalized intercompany agreements pursuant to RCW 48.31B.025(2) and in compliance with RCW 48.31B.030(1)(a)(iv):

- i) Specific methodology on how mortgage loan guarantees and holdback funds are established, released and applied to the sale of mortgage receivables with Metropolitan.
- ii) Interest rate applied or paid to Metropolitan on holdback balances
- iii) Specific methodology on how Metropolitan tracks and applies capitalized underwriting fees and guaranteed yields to applicable sales of mortgage receivables
- iv) Specific methodology on how Metropolitan tracks and applies management fees and servicing rights on the purchase and sales of mortgage receivables.
- v) Intercompany loans or lines of credit by Western to Metropolitan.

The Company was not able to reconstruct several intercompany transactions due to personnel changes and lack of formalized procedures. In some instances it was necessary to back into transactions to understand the methodology used which did not always appear consistently applied. This raises significant concerns as to overall control and oversight of intercompany transactions.

The Company is instructed to file amendments to its intercompany agreement(s) which address areas noted above with the Washington Insurance Commissioner's Office pursuant to RCW 48.31B.030. The agreement should include additional documentation, which explicitly states the services, responsibilities and considerations under the performance of the contract. The amended agreements should also address and correct the deficiencies noted below to maintain compliance with RCW 48.31B.030(1)(a)(iv) which states:

> "The books, accounts, and records of each party to all such transactions must be so maintained as to clearly and accurately disclose the nature and details of the transactions, including such accounting information as is necessary to support the reasonableness of the charges or fees to the respective parties…"

b. Holdback calculation

The Company was not able to provide supporting documentation or calculations to verify the stated number of basis points used as a holdback for loans purchased under the guaranty. As a result, they were not able to verify the initial holdback amount established for all the pool years, which amounted to ($38,760,707). It attempted to verify the amount of holdback initially established on 1997 mortgage purchases subject to underwriting fees. However, it could not provide detailed calculations to support the worksheet. Further, it could not verify the holdback amount on partial mortgage purchases for 1997. Additionally, the Company was unable to provide documentation on the calculations for FYE 1996 to 1998 relating to the amount of holdback released due to securitization sales, which offset the original liability by $25,462,258. The Company is instructed to amend the intercompany agreement to document the methodology and reasonableness of the holdback reserved pursuant to RCW 48.31B.030(1)(a)(iv) as instructed above.

c. Loss reserve interest

Western pays Metropolitan interest on the holdback reserve. The Management, Acquisition and Servicing Agreement between Metropolitan and Western does not contain a clause or guidelines for the payment of interest to Metropolitan on holdback reserves. The Company was able to produce and support interest calculations on the reserve balances for the years under review. The rates applied varied approximately between 8.5% to 10%. The Company is instructed to amend the intercompany agreement to document the methodology and reasonableness of the interest charges applied pursuant to RCW 48.31B.030(1)(a)(iv) as instructed above.

d. Intercompany account reconciliation

Our examination of the receivable and payables to the parent, subsidiaries and affiliates disclosed the Company does not perform reconciliations, but instead maintains a running balance using the net difference at the end of any reporting period as the ending balance. In the absence of account reconciliation, it would be all but impossible to detect all posting and other errors except in obvious or blatant instances.

The Company is instructed to perform intercompany account reconciliations and institute written guidelines that are periodically reviewed for adherence. This will ensure full and adequate accounts and records of its assets, obligations, transactions, and affairs in compliance with RCW 48.05.280 and enhance the credibility and accuracy of future statutory and other filings.

19. Securitizations

The Company pools mortgage loan assets with Metropolitan and other affiliates in order to securitize and sell the mortgage loans under pooling and servicing agreements which create Mortgage Pass-Through Certificates. In order to effectuate these transactions, Metropolitan created Metropolitan Asset Funding, Inc., as the depositor, and utilized the Bank of New York as the trustee. Since 1997 through the present, the Company has participated in numerous separate securitizations. Our review focused on the Metropolitan Asset Funding, Inc. II Mortgage Pass Through Certificates Series 1999-D.

Based on the analysis of the intercompany settlement of the proceeds from this securitization, we have determined the allocation methodology is not in accordance with Washington Statutes. Metropolitan, as the controlling entity, determined the formula used to establish the basis for distribution of proceeds. This formula calculated numerous elements of the securitization distributions between affiliates, such as accrued interest, discounts, premiums and servicing basis. The servicing basis included a servicing right and ancillary income components. The servicing rights asset was distributed based on the proportional contribution of each participant in the securitization. However, ancillary income was distributed in its entirety to Metropolitan.

All of the securitizations participated in by Western exceeded the 3% threshold of admitted assets in which prior approval is required pursuant to RCW 48.31B.030(1)(b). Western did not receive prior approval. Prior approval would have only been granted if the transactions met the standards set forth in RCW 48.31B.030(1)(a), which states:

> "Transactions within a holding company system to which an insurer subject to registration is a party are subject to the following standards;
> (i) The terms must be fair and reasonable;
> (ii) Charges or fees for services performed must be fair and reasonable;
> (iii) Expenses incurred and payment received must be allocated to the insurer in conformity with customary insurance accounting practices consistently applied;…"

Customary insurance accounting practices require charges or fees for services performed, expenses paid, and payments received, to be allocated on an actual ***cost*** basis. Metropolitan calculated the future servicing basis of the ancillary income component on the mortgage loans that Western contributed and secured the income component for Metropolitan's own account by reducing Western's proportional distribution from the proceeds of the securitization. Metropolitan bases this on an intercompany agreement Metropolitan was not a party to, i.e. Servicing Agreement between Metwest and Western. Metropolitan, as the controlling entity in the holding company system, used the intercompany transactions to its own benefit in a fashion that would not constitute an "arms length transaction" nor comply with the holding company statutes as stated above.

Western is entitled to its proportional share of the ancillary income component of all securitizations, including those backed with other contract receivables that were securitized. Pursuant to RCW 48.31B.030(1), Western is instructed to calculate its proportion of ancillary income from all securitizations between affiliates, and receive reimbursement from Metropolitan. Additionally, the Company is instructed to cease all intercompany transactions which are not based on customary insurance accounting practices which require charges or fees for services performed, expenses paid, and payments received, to be allocated on an actual *cost* basis, and if applicable, have not received prior approval pursuant to RCW 48.31B.030.

COMMENTS AND RECOMMENDATIONS

1. Risk Based Capital (RBC)

The Company's RBC ratio has experienced negative trending over the period of examination to levels that are very close to company action levels. This is also true of the Company's other insurance affiliates, Old West Annuity and Life Insurance Company and Old Standard Life Insurance Company. The parent, Metropolitan Mortgage and Securities and other non insurance affiliates have purchased preferred stock from the insurance affiliates to bolster capital and RBC ratios. Metropolitan's assets are highly leveraged which would hamper any purchases of preferred stock of insurance affiliates in the future. It is recommended the Company monitor its RBC ratios closely and verify compliance with RCW 48.05.430 and RCW 48.05.435. Additionally, it is recommended the Company develop a RBC action plan to correct the negative trending before it becomes mandatory under RCW 48.05.440(a)(ii).

2. Actuarial Assets, Reserves, and Liabilities

Implementing the following recommendations will result in a more accurate statement of future actuarial assets, reserves, and liabilities:

- The Company should include premiums payable on reinsurance ceded when determining due and deferred premiums on its life insurance policies.

- The Company should reflect the dynamic valuation interest rates found in the Standard Valuation Law in determining reserves on its level-term life insurance policies.

- The Company should report deficiency reserves for its annual renewable term life insurance policies on the appropriate line of Exhibit 8, Part G.

- The Company should take reinsurance ceded reserve credits for sub-standard and deficiency reserves on its coinsured annual renewable term life insurance policies.

- The Company's reserve calculation for the non-deduction of deferred fractional premiums should reflect all of the Company's deferred premiums.

- The Company's reserve calculation for the immediate payment of claims should reflect the death payment provisions of its life insurance policies.

- The Company should report the reserves for its deferred annuity contracts so as to reflect the valuation interest rate and mortality basis of the calculations.

3. Home Office Depreciation

The Company did not estimate correctly useful life of the office building. According to NAIC Accounting Practices and Procedures Manual for Life, Accident and Health Insurance Companies, Chapter 4-3, the cost of property included in real estate investment, other than land, shall be depreciated over an estimated useful life. The *estimated useful life* of a depreciable asset is the period over which services are expected to be rendered by the asset (ARB-43, Ch. 9C, par. 5). Useful life of the building, based on the Company's depreciation schedule, appears to be too low (2,500,000/210,000 = 11.9 years). The Company needs to revise an estimate of the building's useful life to a more reasonable and appropriate number. Useful life estimates for different type of assets, published by Internal Revenue Service, can serve as guidelines for this revision. The Company needs to treat this change in estimate of useful life of depreciable asset as a change in accounting estimates with current and prospective method of accounting (APB-20, par.10).

4. Pension Fund Determination

The Internal Revenue Service (IRS) has determined and informed the Company by letter dated June 12, 1995 that the Pension Plan and related trust are designed in accordance with applicable section of the Internal Revenue Code (IRC). The Plan has been amended since receiving the determination letter. It is recommended the Company resubmit the Plan to the IRS for determination in order to ensure compliance with IRC statutes and regulations.

HISTORY

The Company was incorporated on June 3, 1963 as a stock life insurance company under the laws of the State of Washington. The Company is owned by Consumers Insurance Company, Inc. and Metropolitan Mortgage & Securities Co., Inc., which own 75.5% and 24.5%, respectively. The Company is strictly a proprietary stock life insurance company authorized to transact life insurance in 15 states. The Company primarily writes deferred and immediate annuity contracts. Additionally, it writes single-premium whole life, interest-sensitive whole life, and traditional life insurance policies.

MANAGEMENT AND CONTROL

Directors & Officers

Directors	Officers	
John Van Engelen	John Van Engelen	President
C.Paul Sandifer Jr	Reuel Swanson	Secretary

Bruce Blohowiak	Jon McCreary	Acting Treasurer
Reuel Swanson	William Zehner	VP Actuary
Irv Marcus	C.Paul Sandifer Jr	VP
	Dale Whitney	VP
	Bruce Blohowiak	VP
	Linda Mason	VP
	Scott Cordell	VP
	David Luhn	VP, Controller

Affiliated Companies

The Company is a member of a holding company system regulated pursuant to RCW Chapter 48.31B. Within the holding company structure, Metropolitan controls numerous affiliates with various functions, including but not limited to, property development, mortgage loan origination and purchasing, the servicing of mortgages and structured receivables, and venture capital financing. In addition to the insurance affiliates listed below, C. Paul Sandifer, Jr., as an individual, owns National Summit Corporation, which through a system of holding companies owns Old Standard Life Insurance Company domiciled in Idaho and Old West Annuity Life Insurance Company domiciled in Arizona. C. Paul Sandifer as the controlling stockholder in Metropolitan, exercises full control of Western through direct and indirect stock ownership in the Washington affiliates listed below:

METROPOLITAN MORTGAGE & SECURITIES COMPANY, INC. (Metropolitan), is the parent and controlling company for a number of non-insurance corporations and the Consumers Group Holding Company, Inc., including Consumers Insurance Company, Inc., and Western United Life Assurance Company. Metropolitan was incorporated January 8, 1953, in the state of Washington for purposes of real estate financing, mortgage banking and insurance. Metropolitan owns 96 percent of Consumers Group Holding Company, Inc.

CONSUMERS GROUP HOLDING COMPANY, INC., formerly Metro Management Corporation, a Washington Corporation, was incorporated September 29, 1971, as an insurance holding company. This Company owns 100 percent of Consumers Insurance Company.

CONSUMERS INSURANCE COMPANY, INC. (Consumers), a Washington corporation, formerly Investors Insurance Exchange, was converted to a stock insurer and the current name was taken October 26, 1978. As of August 23, 1984, Consumers Insurance Company, Inc., ceased writing or renewing all auto, general lines and property insurance except mortgage guarantee insurance for the parent, Metropolitan. Consumers owns 24.5% of Western' outstanding common stock with Metropolitan owning the remaining 75.5%.

CAPITAL AND SURPLUS

RCW 48.05.340 requires the Company to maintain minimum levels of unimpaired capital and surplus in order to transact business. The Company is grandfathered under previous capital and surplus requirements prior to June 9, 1994, and is required to maintain only an aggregate amount of paid-in capital stock or basic surplus of $150,000 and additional surplus of $150,000. The Company has maintained an excess of these amounts over the period under examination.

Common Stock

The Company's Board of Directors has authorized five million shares of one dollar par common stock. As of December 31, 1999, $2.5 million of common stock was issued and outstanding. Metropolitan Mortgage & Securities and Consumers Insurance Company owns 1,887,500 and 612,500, respectively, of the 2,500,000 outstanding shares.

Preferred Stock

The Company's Board of Directors authorized five million shares of non-voting, non-cumulative, and non-convertible ten dollar par preferred stock. As of December 31, 1999, the Company had issued 3,460,000 shares for $34,600,000 dollars with an interest rate set at prime plus one. Metropolitan Mortgage & Securities and Consumers Insurance Company owns 3,110,000 and 350,000, respectively, of the 3,460,000 outstanding shares. The Company paid $1,577,917 in dividends on preferred stock in 1999.

Surplus Notes

The Company retired surplus notes payable to Consumers Insurance Company and Metropolitan in the amounts of $3.5 million and $27.3 million, respectively. The surplus notes carried various annual interest rates of between prime plus three points and 12%. Surplus notes interest was payable only out of earned surplus (as defined in RCW 48.08.030) and at such times as the Company maintained a Risk Based Capital (RBC) above 350%. The surplus notes were replaced by the sale 30,800,000 shares of preferred stock to Metropolitan and Consumers in 1999. The Company paid $1,970,561 in interest on surplus notes in 1999.

CONFLICT OF INTEREST

The Company has a policy statement regarding conflicts of interest. All Directors, Officers, and key employees are required to complete conflict of interest statements. No conflicts were noted for the six years under examination.

CORPORATE RECORDS

Review of the minutes of the Board of Directors of the Company for the period under examination did not indicate any material changes to the corporate Bylaws and the Articles of Incorporation. The minutes of the meetings of stockholders, directors and committees adequately approve and support Company transactions and events. All corporate records are maintained in Spokane, Washington at Metropolitan's home office.

FIDELITY BONDS AND OTHER INSURANCE

Fidelity bonds and other insurance were reviewed to ensure the Company has adequately identified and maintained coverage for property and liability claims that may arise out of the ordinary course of business. Our examination determined the Company has adequately insured itself against unforeseen property and liability exposures and fidelity bond coverage for directors, officers, and key employees. Additionally, the Company's fidelity bonds and other insurance meet or exceed all statutory and/or NAIC minimum guidelines to protect Company assets and policyholders.

WELFARE AND PENSION PLANS

Pension Plan

Western employees are covered by a qualified defined contribution pension plan (401k) sponsored by the Company's parent, Metropolitan. Contributions of up to fifteen percent per year may be made by eligible employees. Metropolitan may match one-half of these contributions up to six percent. The Company has made adequate provision within its financial statements to account for obligations under the pension plan. (See "Comments and Recommendations 4")

Deferred Compensation Plan

Certain qualified Company officers and employees are eligible to participate in a non-qualified deferred compensation plan depending upon their pay scale. This plan is sponsored by Metropolitan. Under the terms of this plan, participants contractually agree to defer a portion of their compensation to a later date. The plan is fully funded, but contributions are subject to the general creditors of Metropolitan, and as such future payments are not guaranteed.

TERRITORY AND PLAN OF OPERATION

The Company is currently licensed to do business in the following fifteen states:

Alaska	Arizona	Hawaii	Idaho	Indiana	Montana
Nebraska	Nevada	North Dakota	Oregon	South Dakota	Texas
Utah	Washington	Wyoming			

Direct premiums were generated in all fifteen of these states during the period covered in this examination. 99.7% of all 1999 direct premiums were written in states that the Company is authorized to transact business. Direct premiums written in unauthorized states is generated from normal migration of policyholders from authorized states. The Company's underwriting, policy preparation, claim settlement, and draft issuance are performed in the Spokane home office.

GROWTH OF THE COMPANY

The growth of the Company is reflected in the following schedules compiled from the Company's Annual Statements as of December 31:

Schedule 1	1999	1998	1997	1996	1995
Total admitted assets	$891,833,300	$885,696,127	$932,343,121	$916,126,393	$865,391,854
Total liabilities	832,092,340	825,894,515	880,137,177	866,062,656	819,175,428
Aggregate life reserves	790,540,151	784,420,100	805,158,797	827,649,924	780,230,285
Asset valuation reserve	8,000,000	6,500,000	6,372,910	6,381,938	5,570,891
Capital:					
Common stock	2,500,000	2,500,000	2,500,000	2,500,000	2,500,000
Preferred stock	34,600,000	3,800,000			
Surplus notes		30,800,000	30,800,000	30,800,000	30,800,000
Gross paid in contributed surplus	9,855,000	9,855,000	9,855,000	9,855,000	9,855,000
Unassigned funds	12,785,960	12,846,612	9,050,944	6,908,737	3,061,426
Total capital and surplus	**$59,740,960**	**$59,801,612**	**$52,205,944**	**$50,063,737**	**$46,216,426**

Risk based capital (RBC)	**302%**	**381%**	**351%**	**382%**	**380%**
RBC 12/312000	**296%**				

Schedule 2	**1999**	**1998**	**1997**	**1996**	**1995**
Premium income:					
Ordinary individual annuities	$113,049,225	$104,613,491	$80,353,125	$122,742,400	$182,809,755
Ordinary life insurance	1,514,054	1,732,813	1,929,305	2,165,826	2,510,842
Total premium income	114,563,279	106,346,304	82,282,430	124,908,226	185,320,597
Investment Income:					
Net investment income	66,275,726	60,445,119	63,248,781	69,163,808	65,852,363
Realized capital gains (losses)	(5,788,030)	2,473,742	808,883	220,432	572,589
Unrealized capital gains (losses)	1,104,445	(3,933,532)	(2,482,268)	(1,440,051)	(467,530)
Total investment income	61,592,141	58,985,329	61,575,396	67,944,189	65,957,422
Benefits and reserve changes:					
Death benefits	1,993,429	1,440,193	1,277,482	1,222,487	1,166,864
Annuity benefits	27,835,945	26,690,468	25,918,083	21,264,187	18,964,219
Disability benefits	5,446	7,572	4,835	8,126	4,298
Surrender benefits	124,154,747	146,342,551	125,297,090	103,145,799	128,251,031
Change in life and A&H reserves	6,120,051	(20,738,697)	(22,491,127)	47,419,639	81,960,540
Total benefits and reserve changes	160,109,618	153,742,087	130,006,363	173,060,238	230,346,952
Total operating and other expenses	10,671,417	11,522,065	11,077,649	15,573,123	17,963,495
Net gain (loss) from operations	12,636,800	5,855,994	7,806,828	7,101,187	4,968,306
Net income (loss)	**$2,773,202**	**$7,806,676**	**$4,640,379**	**$6,137,759**	**$5,202,237**

BUSINESS IN FORCE BY STATES

The following schedule reflects direct written premiums by the Company for the year ended December 31, 1999:

AK	$471,638	ID	$50,921,737	NC	$191,539	PA	$125,000
AL	100,000	IL	445,203	ND	8,200,850	SD	583,767
AR	58,574	IN	150,000	NE	520,898	TN	691,748
AZ	2,272,022	KS	377,404	NH	125,000	TX	591,517
CA	4,316,222	LA	100,000	NJ	175,000	UT	19,935,177
CO	1,730,761	MA	100,000	NM	299,779	VA	698,195
CT	25,000	MD	231,732	NV	3,045,501	WA	111,799,227
FL	1,877,239	MI	189,210	NY	30,000	WI	440,177
GA	35,000	MN	2,229,670	OH	446,887	WY	2,182,414
HI	21,948,596	MO	306,698	OK	232,537	Other	498,781
IA	160,466	MT	6,619,786	OR	23,109,466		

Total Business in Force by State **$268,590,418**

AGGREGATE RESERVE FOR LIFE POLICIES AND CONTRACTS

Aggregate reserves for life policies and contracts were reviewed and attested to by Thomas L. Burger, FSA, MAAA, Senior Consulting Actuary, Taylor-Walker & Associates, Inc. Mr. Burger was retained and contracted for participation in the examination of Western United Life Assurance Company by the Montana Department of Insurance. In addition, Dennis M. Stanley, FSA, Consulting Actuary, Milliman & Robertson, Inc., was retained by the Company to perform independent actuarial analysis over the six years under examination in order to issue an actuarial opinion in compliance with RCW 48.74.025 and WAC 284-07-360.

Aggregate reserves for life policies and contracts were reviewed on a net and gross basis of reinsurance. Mr. Burger determined aggregate reserves for life policies and contracts and other related balance sheet accounts overstated assets by $36,032 and overstated liabilities by $4,797,235 for a net increase in capital and surplus of $4,761,203. These are disclosed in the "Instructions" portion of the examination report.

We reviewed the Statement of Actuarial Opinion and the supporting Actuarial Memorandum regarding the Company's asset adequacy analysis. These documents were submitted with the Company's 1999 Annual Statement as provided for in Section 3 of the Standard Valuation Law, and in Section 8 of the NAIC Model Actuarial Opinion and Memorandum Regulation. Based upon cash flow testing, the Company's consulting actuary concluded that:

> "The reserves and related items, when considered in light of the assets held by the Company with respect to such reserves and related actuarial items including, but not limited to, the investment earnings on such assets, and the considerations anticipated to be received and retained under such policies and contracts, make adequate provision, according to presently accepted actuarial standards of practice, for the anticipated cash flows required by the contractual obligations and related expenses of the Company."

A cash flow projection is a complex combination of inter-related calculations that is difficult to verify. Our review involved evaluating the assumptions used to prepare the cash flow projection, and evaluating the resulting patterns found in the projection in light of these assumptions. Our review found that the cash flow projections were prepared in a consistent manner, and that the projections support the consulting actuary's conclusions concerning the adequacy of the Company's reserves.

However, during our review of the cash flow projections for 1998 and 1999, we noted that the matching relationship between the Company's projected assets and liabilities during the next five calendar years is deteriorating. The 1999 projections indicate that short-term cash flow deficits are predicted to occur under the level interest rate and increasing interest rate scenarios. These deficits will need to be funded from anticipated positive cash flows from new business, by borrowing from outside sources, or from the sale of existing assets.

REINSURANCE

The Company currently has nineteen active ceded reinsurance treaties in effect with nine different reinsurers. There are sixteen automatic and three facultative treaties. The treaties provide coverage for annuities, life, accidental death and disability in excess of the Company's retention. The current retention limits on life products range up to one hundred thousand dollars with reinsurer limits up to three million. As of December 31, 1999, the Company reported the following:

Premiums ceded	$14,496,982
Reserve credits taken	91,356,438
In force at year end	41,830,551

Approximately ninety eight percent of ceded premiums and ninety nine percent of reserve credits are ceded to Old Standard Life Insurance Company, an affiliate, under an automatic single premium deferred annuity coinsurance contract. Under the terms of this contract, the Company retains twenty five percent and cedes seventy five percent of all gross premiums, policy reserves, policy claims and benefits, and commissions incurred.

Reinsurance agreements were reviewed for compliance with Washington State reinsurance statutes. In addition, all reinsurers were verified as authorized or unauthorized and noted if properly classified in schedule F. Reserve credits were reviewed and verified during the actuarial phase of our examination. Based on our review, the Company appears to be adequately monitoring its reinsurance program, including the financial condition of reinsurers and the overall reinsurance program appears to be adequate for the Company's exposure and ability to assume risk.

ACCOUNTS AND RECORDS

The Company's accounts and records are maintained on a Generally Accepted Accounting Principles (GAAP) basis of accounting and are converted to Statutory Accounting Practices (SAP) accrual basis for reporting purposes. The Company is audited annually by the Certified Public Accountants, PricewaterhouseCoopers, LLP. PricewaterhouseCoopers, LLP, issued an unqualified opinion for 1999. Several control and recording deficiencies led to an inability by the Company to supply and support certain requested information on intercompany transactions and mortgage loan assignment activity. These items are discussed in the "Instructions" portion of the examination report.

ELECTRONIC DATA PROCESSING SYSTEMS AND OPERATIONS

The Management of Western is sufficiently knowledgeable of EDP issues and the various department managers work with the IS Department to provide direction and oversight. Systems Development, Acquisition and Maintenance Controls were evaluated to gain assurance that programs and systems are designed, tested, approved and implemented using appropriate controls. The Company has detailed written documentation for its major operations and financially significant applications. Proper supervision and review exist for each project to ensure satisfactory completion. The Company has an Internal Audit Department, but does not have an IS Specialist within the Internal Audit Department. Instead, Metropolitan obtains external auditors to provide system reviews.

The Company's EDP services are provided by Metropolitan. Operations, processing and documentation controls were reviewed to determine the type of hardware installed; operating systems and proprietary software in use; back up and recovery facilities employed and the controls exercised to maintain data security. Adequate procedures and controls are in place for its mainframe operations, PC's and Year 2000 issues.

The Company has completed testing of its EDP Systems to verify financially significant applications are in compliance with Year 2000 issues. In the event of any unforeseen circumstances, the Company has prepared a detailed written contingency plan to ensure its ability to service the needs of its policyholders.

SUBSEQUENT EVENTS

1. Personnel Changes

The following changes have taken place with regard to certain key and Executive Officers:

Bruce J. Blohowiak	Resigned as Executive Vice President, Corporate Counsel and Director of Metropolitan Mortgages & Securities Co., Inc. effective January 28, 2000. Mr. Blohowiak also resigned as Vice President and Director of Western United Life Assurance Company effective January 28, 2000.
Steven Crooks	Resigned as Vice President and Controller of Metropolitan Mortgage & Securities Co.,

	Inc., effective January 28, 2000.
Jon McCreary	Promoted to Vice President/Chief Investment Officer for Metropolitan Mortgage & Securities Co., Inc. Discontinued in the position of acting Treasurer for both Metropolitan Mortgage & Securities Co., Inc., and Western United Life Assurance Company on January 1, 2000. Mr. McCreary remained on the Investment Committee for Western United Life Assurance Company. Mr. McCreary subsequently resigned on July 14, 2000.
Joel Rosenberg	Appointed Treasurer for Metropolitan Mortgage & Securities Co., Inc. and Western United Life Assurance Company effective January 1, 2000. Mr. Rosenberg subsequently resigned on July 15, 2000.
Susan Thompson	Resigned as Assistant Secretary for Metropolitan Mortgage & Securities Co., Inc. effective January 28, 2000. Ms. Thompson handled regulatory affairs for the Metropolitan Mortgage & Securities Co., Inc. group.

2. Surrender Charges

The Company has experienced large surrender payment activity which has contributed to a negative cash flow. Western believes surrender activity will moderate and the negative cash flow will cease for the Company on an overall basis. In 1999, Western paid $148 million in annuity benefits of which $121 million were annuity surrender payments. This was a decrease from the $170 million of annuity benefits and $143 million of annuity surrender payments made in 1998. Through the first nine months of 2000, annuity benefit payments were approaching $190 million of which over $165 million were surrender payments. Of these payments, $67 million, or 40%, were rewritten into new Western deferred annuity contracts. The increase in these payments in 2000 is attributed to the large amount of account value on which the surrender charge will expire in 2000 and the availability of competitive products due to the rise in interest rates in the last year. The former is attributable to the expiration of surrender charges on the contracts written during the high production years of 1991 and 1995. The Company expects annuity surrenders to decline in the year 2001.

Western's termination studies indicate that the persistency rate on deferred annuities immediately after the surrender charge period decreases from that during the surrender charge period. This is a function of the interest rates credited on the contracts, agent behavior, and alternative investments available to policyholders. Many of its agents sell the Company's contracts with the intention of replacing them after the surrender charge period and receiving a new commission. Due to the liquidity of these liabilities after the surrender charge period, the Company must maintain sufficient asset liquidity to cover any cash surrenders. As a result, it cannot earn a sufficient yield that would allow it to credit the same rate of interest as it can on contracts with a long-surrender charge period. Consequently, it must credit a lower rate on contracts after they are out of their surrender charge period. When interest rates rise, this presents the agent and the policyholder with the opportunity to replace a current contract not subject to surrender penalty with a new contract having a higher interest guarantee. For the contracts that were rewritten, Western has experienced this as beneficial as the Company can invest these funds for a longer horizon and at an appreciably better yield.

At the end of 1999, Western had $145 million of annuity values not subject to surrender charge. During 2000, the surrender charges on an additional $137 million of annuity values will have expired. This leaves $282 million of December 1999 annuity values that will not be subject to a surrender charge during 2000. From the summer of 1999 to the spring of 2000, intermediate U.S. Treasury yields increased by about 100 basis points. This increase was also being reflected in the crediting rates of deferred annuity products offered by Western and its competition. Consequently, policyholders were able to surrender existing contacts not subject to a surrender penalty and purchase a new contract with a more favorable crediting rate. This accounts for the increase in surrender activity seen on Western's deferred annuities during 2000. To compensate for this cash outflow, the Company has increased its production levels to about $180 million for 2000. As of September 30, 2000, Western retained $148 million of account value that was not subject to surrender charge and expected that surrender charges will expire in the next twelve months on an additional $112 million of account values. Interest rates are presently declining and barring an unexpected increase in interest rates, this should result in a decline in surrender activity during the next year.

3. Metropolitan Mortgage & Securities Co, Inc., Long-Term Growth Plans

Metropolitan has changed its long-term growth plans and will redirect Company resources to areas of more proven profitability. Some of the strategic alternatives being implemented may include taking the Company out of the traditional residential mortgage industry and its related activities and reallocating those resources to the Company's current and more profitable lines of business, such as commercial lending, property development, and insurance operations or to new strategic opportunities.

Metropolitan will continue to invest in the acquisition and origination of real estate secured receivables, including the Company's seller-financed real estate contract purchases. These investments have been a business of the Company since 1953 and an activity that Metropolitan is known for throughout the real estate industry. In addition, Metropolitan will continue to increase its successful commercial lending operations. Those operations originated over $124 million during the fiscal year ending September 30, 2000, an increase of $59 million over the prior fiscal year. The property development division is also experiencing record growth with $16 million in sales during that same period. In addition, the Company intends to continue to grow its insurance operations in the future.

WESTERN UNITED LIFE ASSURANCE COMPANY
Statement of Assets, Liabilities, Surplus and Other Funds
December 31, 1999

Assets	**Balance Per Company**	**Ref**	**Adjustments**	**Balance Per Exam**
Bonds (Note 2)	$384,253,595			$384,253,595
Stocks:				0
Preferred stocks	50,000			50,000
Common stock	6,162,664			6,162,664
Mortgage loans on real estate - first liens (Notes 3, 12)	392,897,608			392,897,608
Real estate:				
Properties occupied by the company	3,370,759	A1	(100,759)	3,270,000
Properties acquired in satisfaction of debt (Note 4)	14,949,912			14,949,912
Investment real estate (Note 5)	21,088,959	A2	(515,402)	20,573,557
Policy loans (Note 6)	18,971,329			18,971,329
Cash and short term investments (Note 7)	21,916,291			21,916,291
Other invested assets	8,561,753			8,561,753
Receivable for securities	256,623			256,623
Aggregate write-ins for invested assets	53,121			53,121
Amounts recoverable from reinsurers	0			0
Electronic data processing equipment	130,523			130,523
Federal income tax recoverable and interest thereon	4,076,435	A3	629,797	4,706,232
Guarantee funds receivable or on deposit	248,314			248,314
Life insurance premiums and annuity considerations deferred and uncollected	451,803	A4	(36,032)	415,771
Investment income due and accrued	11,329,915			11,329,915
Receivable from parent, subsidiaries and affiliates	277,159	A5	1,752,043	2,029,202
Aggregate write-ins for other than invested assets (Note 8)	2,786,537			2,786,537
Total assets	**891,833,300**		**1,729,647**	**893,562,947**
Liabilities, surplus and other funds				
Aggregate reserve for life policies and contracts	790,540,151	A6	(6,599,917)	783,940,234
Policy and contract claims: life	9,060,302	A7	1,802,682	10,862,984
Premiums and annuity considerations received in advance	13,086			13,086
Liability for premium and other deposit funds: policyholder premiums	1,477,756			1,477,756
Interest maintenance reserve (Note 9)	10,695,442			10,695,442
General insurance expenses due or accrued	0	A8	281,829	281,829
Taxes, licenses and fees due or accrued, excluding FIT	85,549	A9	1,832,639	1,918,188
Unearned investment income	154,842			154,842
Amounts withheld or retained by company as agent or trustee	8,825			8,825
Amounts held for agents' account	60,563			60,563
Remittances and items not allocated	3,180,664			3,180,664
Asset valuation reserve (Note 10)	8,000,000			8,000,000
Payable to parent, subsidiaries and affiliates	3,338,137			3,338,137
Aggregate write-ins for liabilities	5,477,023			5,477,023
Total liabilities	**832,092,340**		**(2,682,767)**	**829,409,573**
Common capital stock	2,500,000			2,500,000
Preferred capital stock	34,600,000			34,600,000
Gross paid in and contributed surplus	9,855,000			9,855,000
unassigned funds	12,785,960		4,412,414	17,198,374
Total surplus and other funds	**59,740,960**		**4,412,414**	**64,153,374**
Total liabilities, surplus and other funds	**$891,833,300**		**$1,729,647**	**$893,562,947**

WESTERN UNITED LIFE ASSURANCE COMPANY
Summary of Operations
For the Year Ended 1999

	Balance Per Company	Ref	Adjustments	Balance Per Exam
Premiums and annuity considerations	$114,563,279			$114,563,279
Net investment income (Note 13)	66,275,726			66,275,726
Amortization of interest maintenance reserve	1,663,659			1,663,659
Commissions and expense allowances on reinsurance ceded	986,961			986,961
Totals	**183,489,625**		**0**	**183,489,625**
Death benefits	1,993,429			1,993,429
Annuity benefits	27,835,945			27,835,945
Disability benefits and benefits under accident and health policies	5,446			5,446
Surrender benefits and other fund withdrawals	124,154,747			124,154,747
Interest on policy or contract funds	71,790			71,790
Increase in aggregate reserves for life and accident and health policies	6,120,051			6,120,051
Commissions on premiums, annuity considerations and deposit type funds	5,107,778			5,107,778
General insurance expenses	4,858,803	A2/A8	797,231	5,656,034
Insurance taxes, licenses and fees, excluding federal income tax	713,518	A9	1,832,639	2,546,157
Increase in loading on and cost of collection in excess of loading on deferred and uncollected premiums	(8,682)			(8,682)
Totals	**170,852,825**		**2,629,870**	**173,482,695**
Net gain from operations before dividends to policyholders and FIT	12,636,800	A2/A8/A9	(2,629,870)	10,006,930
Dividends to policyholders	0			0
Federal income taxes incurred	0	A3	629,797	629,797
Net realized capital gains or losses less capital gains tax & IMR transfers (Note 14)	(9,863,598)			(9,863,598)
Net Income	**2,773,202**		**(2,000,073)**	**773,129**

	Balance Per Company	Ref	Adjustments	Balance Per Exam
CAPITAL AND SURPLUS ACCOUNT				0
Capital and surplus, December 31, 1998	**59,801,612**		**0**	**59,801,612**
Net income	2,773,202		(2,000,073)	773,129
Change in net unrealized capital gains or losses	1,104,445			1,104,445
Change in non-admitted assets and related items	88,239		6,412,487	6,500,726
Change in asset valuation reserve	(1,500,000)			(1,500,000)
Change in surplus notes	(30,800,000)			(30,800,000)
Capital changes: paid in	30,800,000			30,800,000
Dividends to stockholders	(1,577,917)			(1,577,917)
Aggregate write-ins for gains and losses in surplus	(948,621)			(948,621)
Net change in capital and surplus for the year	**(60,652)**		**4,412,414**	**4,351,762**
Surplus as regards policyholders, December 31, 1999	**$59,740,960**		**$4,412,414**	**$64,153,374**

WESTERN UNITED LIFE ASSURANCE COMPANY
Comparative Statement of Assets, Liabilities, Surplus and Other Funds
For December 31,

Assets	**1999***	**1998**
Bonds	$384,253,595	$287,623,700
Stocks:		
Preferred stocks	50,000	0
Common stock	6,162,664	6,674
Mortgage loans on real estate - first liens	392,897,608	405,799,986
Real estate:		
Properties occupied by the company	3,270,000	3,480,000
Properties acquired in satisfaction of debt	14,949,912	14,312,742
Investment real estate	20,573,557	18,332,854
Policy loans	18,971,329	18,481,107
Cash and short term investments	21,916,291	95,628,286
Other invested assets	8,561,753	13,408,681
Receivable for securities	256,623	5,209,342
Aggregate write-ins for invested assets	53,121	0
Amounts recoverable from reinsurers	0	56,000
Electronic data processing equipment	130,523	142,422
Federal income tax recoverable and interest thereon	4,706,232	5,494,707
Guarantee funds receivable or on deposit	248,314	1,105,417
Life insurance premiums and annuity considerations deferred and uncollected	415,771	509,099
Investment income due and accrued	11,329,915	11,935,227
Receivable from parent, subsidiaries and affiliates	2,029,202	0
Aggregate write-ins for other than invested assets	2,786,537	4,169,883
Total assets	**893,562,947**	**885,696,127**
Liabilities, surplus and other funds		
Aggregate reserve for life policies and contracts	783,940,234	784,420,100
Policy and contract claims: life	10,862,984	5,744,211
Premiums and annuity considerations received in advance	13,086	5,664
Liability for premium and other deposit funds: policyholder premiums	1,477,756	1,658,270
Interest maintenance reserve	10,695,442	8,283,533
General insurance expenses due or accrued	281,829	0
Taxes, licenses and fees due or accrued, excluding FIT	1,918,188	83,674
Unearned investment income	154,842	146,074
Amounts withheld or retained by company as agent or trustee	8,825	7,199
Amounts held for agents' account	60,563	47,844
Remittances and items not allocated	3,180,664	2,683,226
Asset valuation reserve	8,000,000	6,500,000
Payable to parent, subsidiaries and affiliates	3,338,137	3,131,543
Aggregate write-ins for liabilities	5,477,023	13,183,177
Total liabilities	**829,409,573**	**825,894,515**
Common capital stock	2,500,000	2,500,000
Preferred capital stock	34,600,000	3,800,000
Surplus notes	0	30,800,000
Gross paid in and contributed surplus	9,855,000	9,855,000
unassigned funds	17,198,374	12,846,612
Total surplus and other funds	**64,153,374**	**59,801,612**
Total liabilities, surplus and other funds	**$893,562,947**	**$885,696,127**

*** = Balances adjusted per examination**

WESTERN UNITED LIFE ASSURANCE COMPANY
Comparative Summary of Operations
For the Years Ended December 31,

	1999*	1998
Premiums and annuity considerations	$114,563,279	$106,346,304
Net investment income	66,275,726	60,445,119
Amortization of interest maintenance reserve	1,663,659	1,567,774
Commissions and expense allowances on reinsurance ceded	986,961	2,846,101
Totals	**183,489,625**	**171,205,298**
Death benefits	1,993,429	1,440,193
Annuity benefits	27,835,945	26,690,468
Disability benefits and benefits under accident and health policies	5,446	7,572
Surrender benefits and other fund withdrawals	124,154,747	146,342,551
Interest on policy or contract funds	71,790	85,152
Increase in aggregate reserves for life and accident and health policies	6,120,051	(20,738,697)
Commissions on premiums, annuity considerations and deposit type funds	5,107,778	6,303,390
General insurance expenses	5,656,034	4,579,709
Insurance taxes, licenses and fees, excluding federal income tax	2,546,157	642,473
Increase in loading on and cost of collection in excess of loading on deferred and uncollected premiums	(8,682)	(3,507)
Totals	**173,482,695**	**165,349,304**
Net gain from operations before dividends to policyholders and FIT	10,006,930	5,855,994
Dividends to policyholders	0	0
Federal income taxes incurred	629,797	2,611,479
Net realized capital gains or losses less capital gains tax and IMR transfers	(9,863,598)	(660,797)
Net Income	**2,000,073**	**7,806,676**

CAPITAL AND SURPLUS ACCOUNT

Capital and surplus, December 31, 1998	**59,801,612**	**52,205,944**
Net income	773,129	7,806,676
Change in net unrealized capital gains or losses	1,104,445	(3,933,532)
Change in non-admitted assets and related items	7,130,523	49,614
Change in asset valuation reserve	(1,500,000)	(127,090)
Change in surplus notes	(30,800,000)	3,800,000
Capital changes: paid in	30,800,000	0
Dividends to stockholders	(1,577,917)	0
Aggregate write-ins for gains and losses in surplus	(948,621)	0
Net change in capital and surplus for the year	**4,351,762**	**7,595,668**
Surplus as regards policyholders, December 31, 1999	**$64,153,374**	**$59,801,612**

*** = Balances adjusted per examination**

WESTERN UNITED LIFE ASSURANCE COMPANY
Five Year Reconciliation of Surplus
For the Years Ended December 31,

	*1999	1998	1997	1996	1995
Capital and surplus, December 31, previous	**$59,801,612**	**$52,205,944**	**$50,063,737**	**$46,216,426**	**$43,819,406**
Net income	773,129	7,806,676	4,640,379	6,137,759	5,202,237
Change in unrealized capital gains or (losses)	1,104,445	(3,933,532)	(2,482,268)	(1,440,051)	(467,530)
Change in non-admitted assets and related items	6,500,726	49,614	(24,932)	(39,350)	(306,920)
Change in asset valuation reserve	(1,500,000)	(127,090)	9,028	(811,047)	(2,030,767)
Changes in surplus notes	(30,800,000)				
Capital changes:					
Paid in	30,800,000	3,800,000			
Transferred from surplus					1,175,000
Surplus changes:					
Paid in					
Change in surplus as a result of reinsurance					
Dividends to stockholders	(1,577,917)				(2,975,000)
Issuance of surplus note	(948,621)				1,800,000
Net change in capital and surplus for the year	**4,351,762**	**7,595,668**	**2,142,207**	**3,847,311**	**2,397,020**
Capital and surplus, December 31, current	**$64,153,374**	**$59,801,612**	**$52,205,944**	**$50,063,737**	**$46,216,426**

*** = Balances adjusted per examination**

Examination Adjustments

December 31, 1999

	(Annual Statement reference)	Debit	Credit
A1	Change in Non-Admitted Assets (Pg 4, Col 1, Ln 37)	$100,759	
	Properties Occupied by the Company (Pg 2, Col 4, Ln 4.1)		$100,759
	See "Instruction" 7		
A2	General Insurance Expense (Pg 4, Col 1, Ln 22)	515,402	
	Investment Real Estate (Pg 2, Col 4, Ln 4.3		515,402
	See "Instruction" 8		
A3	Federal Income Tax Recoverable (Pg 2, Col 4, Ln 14)	629,797	
	Federal Income Taxes Incurred (Pg 3, Col 1, Ln 30		629,797
	See "Instruction" 4		
A4	Unassigned Funds (Pg 3, Col 1, Ln 35)	36,032	
	Life Insurance Premiums and Annuity Considerations Deferred and Uncollected (Pg2, Col 4, Ln 15)		36,032
	See "Instruction" 14		
A5	Receivable from Parent, Subsidiaries and Affiliates (Pg 2, Col 4, Ln 19)	1,752,043	
	Unassigned Funds (Pg 3, Col 1, Ln 35)		1,752,043
	See "Instruction" 6		
A6	Aggregate Reserve for Life Policies and Contracts (Pg 3, Col 1, Ln 1)	6,599,917	
	Unassigned Funds (Pg 3, Col 1, Ln 35)		6,599,917
	See "Instruction" 15		
A7	Unassigned Funds (Pg 3, Col 1, Ln 35)	1,802,682	
	Life Policy and Contract Claims (Pg 3, Col 1, Ln 4.1)		1,802,682
	See "Instruction" 16		
A8	General Insurance Expense (Pg 4, Col 1, Ln 22)	281,829	
	General Expenses Due or Accrued (Pg 3, Col 1, Ln 13)		281,829
	See "Instruction" 3		
A9	Insurance Taxes, Licenses and Fees (Pg 4, Col 1, Ln 23)	$1,832,639	
	Taxes, Licenses and Fees Due or Accrued (Pg 3, Col 1, Ln 14)		$1,832,639
	See "Instruction" 11		

NOTES TO THE FINANCIAL STATEMENTS

1. Accounting Policies

A) Basis of presentation

The financial statements included herein have been prepared in accordance with statutory accounting practices prescribed or permitted by the Washington State Insurance Commissioner's Office, NAIC Annual Statement Instructions, and Accounting Practices and Procedures Manual, and Generally Accepted Accounting Practices (GAAP), respectively, in that order of authority.

B) Bonds

All bonds, if amply secured and not in default as to principle and interest, are carried at amortized cost. Such securities, not amply secured or in default, are carried at market value pursuant to RCW 48.12.170. Premiums and discounts are amortized using the interest method over the term of the bond. Realized capital gains and losses on the disposition of bonds are recognized in operations, net of deferrals into the Interest Maintenance Reserve.

C) Stocks

All common and preferred stocks are valued at market pursuant to RCW 48.12.180. Market value is determined by using published market rates by the Securities Valuation Office of the NAIC. Unrealized capital gains and losses on stocks are charged directly to assigned surplus without adjustment to recognize federal income taxes. Realized capital gains and losses on the disposition of preferred and common stocks are recognized in operations in the period incurred.

D) Real Estate Contracts and Mortgage Notes Receivable

Real estate contracts and mortgage notes receivable held for investment purposes are carried at amortized cost, subject to valuation limitations imposed under Chapters 48.12 and 48.13 of the Revised Code of Washington.

E) Property, Plant and Equipment

Buildings, land, and computer equipment are recorded at cost plus capitalized improvements less depreciation subject to certain statutory limitations. Depreciation is computed on a straight line basis over the estimated life depending on the type of asset and statutory regulations. (See "Comments and Recommendations" number four for further analysis).

F) Policy Loans

Policy loans are carried at the unpaid principle balance of the loan up to the amount of the statutory reserve provided on the related life insurance or annuity policy pursuant to RCW 48.12.010(3).

G) Accrued Investment Income

Accrued investment income is recorded as earned subject to RCW 48.12.010. This includes, but is not limited to, interest on bonds not in default, collateral loan interest not exceeding one year, mortgage loan interest not exceeding eighteen months, rent not in arrears more than three months.

H) Premiums deferred and uncollected

Deferred premiums are recorded in amounts representing the portion earned in the period from the premium due date to the next policy anniversary date. Uncollected premiums are recorded for valued policies that are in their grace period, not exceeding legal reserves and other policy liabilities pursuant to RCW 48.12.010(3).

I) Policy Acquisition Costs

Underwriting or policy acquisition costs such as commissions and general insurance expense applicable to underwriting are written off in the year incurred and not deferred and amortized against future earnings.

J) Non-admitted assets
RCW 48.12.020 defines certain nonallowable assets which are listed as non-admitted in the annual statement. These consist of certain receivables over 90 days past due, prepaid expenses, furnishings, equipment and all electronic data processing equipment not meeting the criteria set forth in RCW 48.12.10(11). The changes in such assets are reflected as adjustments to net worth.

2. Bonds

Bonds are obligations issued by business units, governmental units, and certain non-profit units, and having a fixed schedule for one or more future payments of money. This includes commercial paper, negotiable certificates of deposit, repurchase agreements, collateralized mortgage obligations, mortgage participation certificates, interest-only and principle-only certificates, and equipment trust certificates.

Our examination of bonds focused on existence, ownership and proper valuation in compliance with Chapters 48.12 and 48.13 of the Revised Code of Washington, and in conjunction with the NAIC instructions and guidelines. No exceptions were noted during our review and the reported amortized value appears to be free of material error. The following schedules set forth the quality distribution, maturity periods and distribution of security backing the bonds as of December 31, 1999:

Schedule 1- Quality distribution and maturity periods

Quality	1 year or less	Over 1 year to 5 years	Over 5 years to 10 years	Over 10 years to 20 years	Over 20 years	(1)Totals	Percent of Total
Class 1	$52,436,878	$130,000,103	$51,253,764	$31,234,191	$21,741,878	**$286,666,814**	70.62%
Class 2	4,953,471	26,252,410	21,854,048	21,344,511	10,115,638	**$84,520,078**	20.82%
Class 3	1,897,587	8,252,278	6,925,552	7,132,385	2,293,037	**$26,500,839**	6.53%
Class 4	667,311	2,204,068	1,137,205	1,709,054	990,359	**$6,707,997**	1.65%
Class 5	4,071	19,810	35,088	20,767		**$79,736**	0.02%
Class 6	328,450	852,448	69,631	212,129	15,473	**$1,478,131**	0.36%
Totals	**$60,287,768**	**$167,581,117**	**$81,275,288**	**$61,653,037**	**$35,156,385**	**$405,953,595**	100.00%
% of Bonds	14.85%	41.28%	20.02%	15.19%	8.66%	100.00%	

(1) = Includes $21,700,000 of Short Term Investments

Schedule 2 – Security Backing

	Statement Value
Issuer obligations	$199,371,059
Single class mortgage/asset backed	4,311,515
Multi-class residential mortgage backed	175,118,519
Multi-class commercial mortgage/asset backed	5,452,502
Total Bonds	**$384,253,595**

3. Mortgage Loans on Real Estate

Mortgage Loans on Real Estate consist of first lien mortgages collateralized by residential, commercial and farm real estate properties. The geographical distribution risk profile of mortgages indicated an overall concentration of mortgages located in the Rocky Mountain and Pacific Coastal states, approximately 72%. Historically, this area geographically has been an area of expertise for the Company. The face value of the real estate contracts and mortgage notes range primarily between $15,000 and $300,000. Maturity dates ranged between 2000 and 2029, with a weighted average contractual interest rate of approximately 9.1% as of December 31, 1999.

RCW 48.13.120, requires certain guidelines that limit investments in property to seventy-five percent of fair value, eighty percent of single family residential market value, or ninety percent of the fair value of purchase money mortgages. In addition to loan to value ratios, mortgage loans were tested for existence, ownership and proper valuation to confirm compliance with RCW 48.12.010. Our examination disclosed certain exceptions to mortgage loan to value ratios and ownership title perfection (See “Instruction” number nine for further analysis).

The following schedules denote the statement reported values and type distributions which include the unamortitized portion of the capitalized underwriting fees (See “Note” number twelve for further analysis):

Schedule 1 – Type distribution

	Statement Value
Residential mortgages	$279,263,757
Commercial mortgages	108,399,028
Farm mortgages	5,234,823
Total Mortgage Loans on Real Estate	**$392,897,608**

Schedule 2 – Value distribution

	Statement Value
Face value of discounted and acquired receivables	$354,311,182
Face value of originated receivables	40,830,250
Net unamortized premiums/(discounts)	(1,493,824)
Non-admitted receivable reserve	(750,000)
Total Mortgage Loans on Real Estate	**$392,897,608**

4. Properties Acquired in Satisfaction of Debt

Properties Acquired in Satisfaction of Debt are properties held for sale that have been acquired through the foreclosure of delinquent mortgage loans. Pursuant to RCW 48.12.200, these properties are valued at amounts not exceeding the acquisition cost of the real property or 90% of the fair value of such real property, whichever is less. The properties acquired must be disposed of within five years in compliance with RCW 48.13.170. Our examination tested on a sample basis compliance to applicable statutes, as well as verification of ownership, valuation and existence. Except for an assignment issue corrected during the course of our field work, no exceptions were noted. The following schedule lists the types of properties acquired and remaining unsold as of December 31, 1999:

	Statement Value
Single family dwellings	$8,854,567
Multi-family dwellings	587,021
Commercial properties	3,046,481

Land	1,760,654
Condominium units	701,189
Total Properties Acquired in Satisfaction of Debt	**$14,949,912**

5. Investment Real Estate

Investment Real Estate consisted of property acquired for development which is valued at cost plus capitalized development expenditures. Our review indicated the Company capitalized costs that should have been expensed in the period incurred per the NAIC guidelines (See "Instruction" number eight for further analysis). Additionally, it was noted the geographic non-diversity added additional risk to investment real estate. All properties are located in Eastern Washington, primarily in the Spokane region. The following schedule reflects Investment Real Estate, including examination adjustment as of December 31, 1999:

	Location	Statement Value
Retail shopping plaza	Spokane, WA	$11,339,134
Commercial Business Center	Liberty Lake, WA	5,536,888
Commercial Business Center	Airway Heights, WA	2,801,164
Truck and recreational vehicle center	Pasco, WA	1,067,284
Commercial land	Pasco, WA	344,489
Examination Adjustment A2		(515,402)
Total Investment Real Estate		**$20,573,557**

6. Policy Loans

Policy loans are carried at an amount not exceeding the legal reserve maintained on that policy pursuant to RCW 48.13.190, and do not carry an interest rate in excess of eight percent pursuant to RCW 48.23.085. Life and annuity policy loans were sampled and no exceptions were noted in our examination. The following schedule shows the cumulative total of all policy loans outstanding as of December 31, 1999:

	Statement Value
Life insurance policies	$14,149,875
Annuity policies	4,821,454
Total Policy Loans	**$18,971,329**

7. Cash and Short Term Investments

As of December 31, 1999, cash consisted of petty cash, negotiable checks, bank drafts, cashiers checks and demand deposits. Short term investments consisted of NAIC Class 1 money market mutual funds issued by Fidelity Investments and J.P. Morgan Funds, valued at $11.7 million and $10 million, respectively. Cash has maturities of ninety days or less and short term investments have maturities of one year or less. Our examination of cash and short term investments confirmed the balances, ownership, and valuations with no material exceptions noted. The following is a summary of Cash and Short Term Investments as of December 31, 1999:

	Statement Value
Class I money market funds @ 5.88%	$11,700,000
Class I money market funds @ 5.77%	10,000,000
Cash on deposit with Bank of America	215,523
Cash on deposit with Federal Home Loan Bank	768

Total Cash and Short Term Investments	**$21,916,291**

8. Aggregate Write-ins for other than Invested Assets

Aggregate Write-ins for other than Invested Assets consisted primarily of the remaining holdback reserve from Metropolitan applied to 1999 mortgage loan losses covered under the intercompany Management, Acquisition and Servicing Agreement. (See "Instruction" number six for further analysis) The following is a summary of Aggregate Write-ins for other than Invested Assets as of December 31, 1999:

	Statement Value
State/local tax refunds	$428,231
Recoverable under loss guarantee provisions	2,358,306
Total Aggregate Write-ins for other than Invested Assets	**$2,786,537**

9. Interest Maintenance Reserve (IMR)

The IMR is applied to realized capital gains and losses on fixed income investments, net of applicable taxes, and are deferred into the IMR. The reserve is designed to capture the realized capital gains and losses which result from changes in the overall level of interest rates and amortizes them into investment income over the projected remaining term of the investments sold. The Company uses the NAIC approved Grouped Method. Our examination indicated the Company has adequately reserved and calculated the IMR in accordance with the instructions mandated by the NAIC. The following schedules represents the activity through the IMR in 1999:

Schedule 1- 1999 IMR Activity

	Statement Value
Beginning balance 12-31-98	$8,283,533
Realized capital gains transferred, net FIT	4,075,568
Amortization into income	(1,663,659)
Ending balance 12-31-99	**$10,695,442**

Schedule 2 – Realized Capital Gains Transferred to IMR

	Statement Value
Special Revenue and other bonds	$54,859
Real estate contracts and mortgage notes	3,981,932
Other invested assets	38,777
Total Realized Capital Gains Transferred to IMR	**$4,075,568**

10. Asset Valuation Reserve (AVR)

The AVR is designed to address the credit-related (default) and equity risks of the Company's assets by calculating a basic contribution, a reserve objective, and a maximum reserve amount and controlling the flow of the reserve to and from surplus. The default component includes long and short-term bonds, preferred stock, derivative instruments, and mortgage loans. Securities backed by the full faith and credit of the U.S. Government are exempt. The equity component consists of common stock, real estate and other invested assets. Our examination indicated the Company has adequately reserved and calculated the AVR in accordance with the instructions mandated by the NAIC. The following schedule represents the activity through the AVR in 1999:

	Statement Value
Beginning balance 12-31-98	$6,500,000
Net realized capital gains (losses)	(9,863,598)
Unrealized capital gains (losses)	1,104,445
Basic contribution	3,603,591
Accumulated balance	1,344,438
Required additions to reserve	3,135,572
Adjustments and voluntary contributions	3,519,990
Ending balance 12-31-99	**$8,000,000**

11. Borrowed Money $ -0-

The Company has a borrowing agreement with the Federal Home Loan Bank of Seattle in the authorized amount of $88 million dollars. All advances are subject to collateral requirements and bear interest at fixed or variable rates, determined at the date of withdrawal. This agreement remains in effect until written notice of either party. In accordance with the terms of the agreement, the Company must maintain a minimum investment in the common stock of the Federal Home Loan Bank of Seattle. This investment is recorded as restricted common stock with a valuation of $2,760,000 as of December 31, 1999.

The Company typically uses its borrowing capacities to fund structured settlements, real estate contracts, and mortgage notes receivable on a short term basis in order to securitize asset backed obligations in pooled arrangements with Metropolitan and other selected affiliates. In 1999, the Company borrowed approximately $170,227,000 and repaid all amounts outstanding within the year. No amounts were outstanding as of December 31, 1999.

12. Capitalized Underwriting fees $ 18,136,000

Western received approval from the Washington State Insurance Commissioner's Office to capitalize the underwriting fee charged by Metropolitan Mortgage & Securities associated with the sale of real estate contracts and mortgage notes receivable to the Company prior to April 1, 1998, and to amortize this fee over the remaining lives of the real estate contracts and mortgage notes acquired. Under subsequent negotiations with the Washington Insurance Commissioner's Office, the Company suspended the permitted practice of capitalizing underwriting fees on April 1, 1998, and agreed to amortize the existing capitalized costs over a period not exceeding 6.75 years or year ended 2004. The capitalized underwriting fees remaining as of December 31, 1999, increased statutory surplus by approximately $18.1 million.

13. Net Investment Income

The following is a summary of Net Investment Income earned for the year ended 1999:

	Statement Value
U.S. Government bonds	$2,578,897
Other bonds	26,515,473

Common stocks	4,220
Mortgage loans	43,600,410
Real estate	838,657
Premium notes, policy loans and liens	1,367,433
Short term investments	1,174,339
Other invested assets	2,114,334
Other miscellaneous interest	146,675
Gross Investment Income	**78,340,438**
Investment expenses	(12,064,712)
Net Investment Income	**$66,275,726**

14. Net Realized Capital Gains (Losses) less FIT and IMR transfers

The following is a summary of Net Realized Capital Gains (Losses) less federal income tax and interest maintenance reserve transfers for the year ended 1999:

	Statement Value
Bonds	($2,037,158)
Real estate contracts and mortgage notes	(2,656,651)
Real estate	2,923,444
Other invested assets	(4,017,665)
Amounts deferred to IMR	(4,075,568)
Net Realized Capital Gains (Losses)	**($9,863,598)**

ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the Administrator and employees

of the Company during the course of this examination.

In addition to the undersigned, acknowledgment is made of the participation in the work and preparation to this report by Patrick McNaughton, Chief Examiner; Jim Tompkins, Assistant Deputy Commissioner; John R. Jacobson, AFE, Senior Examiner; Constantine Arustamian, CPA, Examiner; all from the Washington State Insurance Commissioner's Office.

Respectfully Submitted,

____

Michael V. Jordan, CPA, CFE, MHP
Examiner-in-Charge
State of Washington

____

Thomas L. Burger, FSA, MAAA
Taylor-Walker & Associates, Inc.
Department of Insurance, Montana
Representing:
Western Zone – NAIC

____

Mark A. Giffin, CFE
Department of Consumer & Business Services, Oregon
Representing:
Western Zone – NAIC

AFFIDAVIT

STATE OF WASHINGTON)
) ss
COUNTY OF THURSTON)

Michael V. Jordan, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

Michael V. Jordan, CPA, CFE, MHP
Examiner-in-charge

Subscribed and sworn to before me this _____ day of ________ , 2001.

Notary Public in and for the
State of Washington, residing
at Seattle.